

Testimony of Darien Shanske
Proposed Bill No. 5673
(Digital Advertising Services Tax)
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I am honored to have the chance to provide this short testimony with you today concerning digital advertising taxes. This testimony is drawn from this co-written article: Christine Kim and Darien Shanske, [*State Digital Services Taxes: A Good and Permissible Idea \(Despite What You Might Have Heard\)*](#), 98 *Notre Dame Law Review* 741 (2022).

There are many policy arguments in favor of a digital advertising tax. I will focus on the one most relevant to legal analysis: a digital ad tax is a tax on otherwise untaxed consumption. The sales is supposed to tax all final consumption. Thus, if I purchase a book of maps in Connecticut, then I am subject to the sales tax. Also, if I download an e-book in Connecticut, then I am [subject to the sales tax](#). However, if I download a free map app, such as Google Maps, I would not be charged sales tax even though I am also engaging in consumption and paying for that consumption through, for example, providing my data. There is a general reason for not taxing barterers that should otherwise be subject to tax and that is that it is hard to assess the monetary value of the sale. In the context of digital ads, we have a reasonable proxy for the value of the sale; it is the value of data I provided when sold by the digital platform in a monetary transaction to advertisers. Thus a digital advertising tax is using the gross receipts from advertising as a proxy to tax transactions that should be part of the sales tax.

This justification for a digital advertising tax does not originate with me or with lawyers. For example, here are two leading tax economists making the same point in 2021:

Four arguments for taxing advertising and consumer sales are provided. First, and the strongest argument, advertising revenues could operate as a surrogate for the implicit value of consumer services . . .

David R. Agrawal & William F. Fox, *Taxing Goods and Services in a Digital Era*, 74 *National Tax Journal* 257, 294 (2021).

Moreover, this analytic point is understood by participants in the industry. Here is one such participant noting that shifting from a subscription model to a barter model can save businesses from the obligation to collect the sales tax – unless a state has a digital ad tax as a backup.

If free and reduced-cost streaming does take a bite out of retail receipts—and by extension, tax collections—state and local legislators may already have a model solution in front of them: tax the ads themselves. In February 2021, Maryland enacted a first-of-its-kind “digital ads tax” targeting the revenue of technology platforms that generate a substantial amount of receipts from advertising in the state.

Toby Bargar, [*Changes to Streaming Media Monetization Could Affect State Taxes*](#), Bloomberg Tax (Oct. 13, 2022). Thus, if a state does not impose a digital ad tax to patch up its current tax base, it might find itself with an even bigger gap in the future because businesses might shift to barter.

Maryland’s first in the nation digital ad tax was found preempted and unconstitutional a few months ago. There can be no guarantees (except of further litigation!), but I do not think this initial determination by a trial court in Maryland should be considered dispositive. For instance, that court did not really address the argument just made concerning the digital ad tax as a backup sales tax. The strongest argument against digital ad taxes is that they discriminate against electronic commerce, in violation of the Internet Tax Freedom Act, but, as just explained, the digital ad tax is not treating digital goods and services worse than others, but trying to treat them the same. Indeed, the digital ad tax is trying to level the playing field between digital barter and the purchase of digital goods already subject to the sales tax in Connecticut.

Two further points about the law. First, the Maryland trial court’s decision was so brief and questionable that the Maryland Supreme Court agreed to hear an appeal directly – without waiting for an intermediate appellate court to weigh in. This is not to say that the Maryland tax will ultimately prevail, only that it is not dead yet and the likelihood of the lower court being overruled on at least procedural grounds seems fairly high. Second, there are some inessential, though defensible, features of the Maryland tax that Connecticut can avoid and thus a Connecticut tax would likely be in a stronger legal position.

Thank you for this opportunity. Please reach out if I can answer any questions.